



Order 96-7-18

**UNITED STATES OF AMERICA
DEPARTMENT OF TRANSPORTATION
OFFICE OF THE SECRETARY
WASHINGTON, D.C.**

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U.S.-Toronto Second Year Service Proceeding

Docket OST-95-782

FINAL ORDER ISSUING CERTIFICATES

By this order, we make final our tentative decision to grant certificate authority to Continental Airlines, Inc. (Continental) and USAir, Inc. (USAir) to operate two daily round-trip scheduled combination frequencies each, Continental between Newark and Toronto and USAir between Washington, D.C. (National) and Toronto. We also make final our tentative decision to grant backup authority to Northwest Airlines, Inc. (Northwest) (as backup to both Continental and USAir) to operate two daily round-trip scheduled combination frequencies between Minneapolis/St. Paul and Toronto.

Background

This proceeding arises from the 1995 air services agreement between the United States and Canada ("Agreement") that provides for expanded economic opportunities in the U.S.-Canada aviation market, including new service to Toronto that is being phased in over a three-year period. During the first year from the date of the Agreement, the Department ultimately selected Delta Air Lines, Inc. (Delta) to operate between Atlanta and Toronto and Trans World Airlines, Inc. (TWA) to operate between St. Louis and Toronto, with each carrier able to operate up to two daily round-trip frequencies.¹ In light of the expanded economic opportunities available under the Agreement during the second year, the Department instituted this proceeding to select two additional carriers to provide scheduled combination service in the U.S.-Toronto market. By Order 96-2-45, as later modified by Order 96-5-21, we tentatively decided to grant the applications of Continental and USAir to serve Newark-Toronto and Washington, D.C. (National)-Toronto, respectively, and tentatively granted backup authority to Northwest (as backup to both Continental and USAir) to operate between Minneapolis/St. Paul-Toronto. Interested parties were directed to show cause why we should not make the tentative decision final.

¹ See Order 95-11-1 and Order 96-5-21 for a full description of the circumstances surrounding the first year awards.

² In Order 96-2-45 we tentatively selected TWA to serve between St. Louis and Toronto. As a result of the subsequent activation of TWA's backup authority to serve that market as a year-one selection, however, the tentative selection of TWA in this proceeding became moot. Order 96-5-21 tentatively selected Continental to replace TWA as the second year-two carrier, and tentatively selected Northwest for backup authority behind both USAir and Continental.

Objections to the tentative decision were received from Midway and the Raleigh-Durham Airport Authority and Northwest.³ Midway and the Raleigh-Durham Airport Authority opposed the order, arguing that the tentative selection ignores Department policy of fostering new entrant carriers, and fails to maximize potential competitive benefits. Midway and the Raleigh-Durham Airport Authority argued that Department policy in this proceeding should focus on awarding new authority in markets before Canadian flag carriers begin service. Northwest argued that the tentative selection is “contrary to law, the record evidence and the public interest.” More specifically, Northwest argued that it would provide a stronger new competitive challenge than USAir to both the Canadian and larger U.S. carriers now serving U.S.-Toronto markets, and that selection of USAir would waste a valuable bilateral right, given USAir’s smaller total traffic forecast. Northwest went on to urge the Department to institute a proceeding immediately using expedited procedures to award third-year Toronto authority in order to provide the carriers selected ample time to prepare for initiation of service in February 1997.

Comments in support of the tentative decision were received from Continental and USAir. These parties countered the various arguments of Midway and Northwest, arguing that the tentative decision followed the decisional criteria articulated in the instituting order and afforded an appropriate amount of weight to the issue of competition with Canadian flag carriers in targeted city-pair markets where the U.S. flag competitive response remains constrained. The answers also rejected Midway’s and Northwest’s assertions that the awards do not maximize competition in the U.S.-Toronto market and service benefits to the traveling and shipping public. Continental, however, embraced Northwest’s suggestion to proceed immediately with the third-year case.

³ While Northwest filed in opposition to both Order 96-2-45 and Order 96-5-21, Midway filed in opposition only to Order 96-2-45. Many of the objections raised by Midway to Order 96-2-45 were not affected by Order 96-5-21, and we therefore address those issues here. The objections raised by Midway that are no longer relevant as a result of Order 96-5-21, along with the objections filed by Continental and the Answers filed by TWA and the St. Louis Parties in response to Order 96-2-45, are moot, however, and not addressed here.

⁴ While Northwest believes that the record supports its selection for primary authority, it characterizes its tentative selection for backup authority on both year-two routes over Midway as “indisputably correct.” Objection of Northwest, at 2.

Decision

We have decided to make final our tentative findings and conclusions in Order 96-2-45, as modified by Order 96-5-21, to grant primary authority to Continental and USAir, and backup authority to Northwest. In taking this action, we conclude that the public interest is best served here by selecting carriers that will offer the strongest head-to-head competition with Canadian carriers in important U.S.-Toronto city-pair markets. Continental and USAir will provide new nonstop service at geographically well situated, major hub airports that otherwise would have only Canadian flag service.

Canadian flag carriers currently provide six daily roundtrip frequencies at Newark, five daily roundtrip frequencies at Washington, D.C. (National), and three daily roundtrip frequencies at Washington, D.C. (Dulles) (where there is currently no U.S. flag service). In contrast, Canadian flag carriers currently provide only four daily roundtrip frequencies at Minneapolis/St. Paul and provide no service at Raleigh-Durham. The selection of Continental and USAir in this proceeding will maximize competition in eastern markets that account for nearly 75 percent of all U.S.-Toronto traffic and where Canadian flag carriers now have 19 gateways serving Toronto. We also conclude that the applications of Continental and USAir provide the greatest overall service benefits.

None of the objectors has presented any arguments that persuade us to adopt their proposals or to change our proposed awards. Indeed, for the most part, the parties reiterate arguments already presented and considered in reaching our tentative decision in this case. Although there are benefits to the service proposals of Midway and Northwest, we find that those benefits are outweighed by the benefits offered by the proposals of Continental and USAir.

Midway and the Raleigh-Durham Airport Authority contend that the Department ignored its own policy favoring new entrant carriers and the selection criteria established for this proceeding (increasing the level of competition among U.S. flag carriers) by selecting USAir, currently the dominant U.S. carrier in the U.S.-Toronto market. Furthermore, Midway and the Raleigh-Durham Airport Authority claim the Department should focus on awarding authority in markets before Canadian carriers begin service, in order to allow U.S. carriers to gain a competitive advantage by establishing their market identity free from Canadian flag competition.

Contrary to Midway's and the Raleigh-Durham Airport Authority's assertions, we have not ignored our policy favoring new entrant carriers or the decisional criteria we established for this proceeding. Indeed, the selection of Continental will introduce service by a new entrant U.S. flag carrier that does not serve the U.S.-Toronto market with its own aircraft.

As we have indicated, in selecting carriers to provide the service at issue, our principal objective is to maximize the public benefits that can be expected to result from awarding this new authority. In reaching our decision in this case, we placed primary emphasis on the effects of the applicants' service proposals on the overall market structure and the level of competition, both between U.S. and Canadian flag carriers and among U.S. flag carriers in the U.S.-Toronto market, in order to promote an air transportation environment that will sustain the greatest public benefits. We also considered which carriers are most likely to offer and maintain service that provides the maximum benefits to the traveling and shipping public. Finally, we considered other factors historically considered in carrier selection where they were relevant.

This proceeding offered us the choice of two of four carriers and gateway points. We have concluded that the selection of Continental and USAir most effectively achieves the most public interest benefits meeting the selection criteria of this proceeding. More specifically, we find that the proposals of Continental and USAir offer the strongest competition to foreign-flag carriers in the

U.S.-Toronto market. In addition, the selection of Continental and USAir benefits passengers and shippers in the two most important U.S.-Toronto markets, providing new nonstop U.S. flag service at major airports without U.S. flag service to Toronto, and linking our nation's largest city and our nation's capitol with Canada's principal traffic point and largest city.

In assessing the competitive impact of each carrier's proposal, we considered the issue of competition among U.S. carriers, and of competition between U.S. carriers as a class and their foreign competitors. In this case, contrary to Northwest's assertions, selection of Continental and USAir maximizes competition between U.S. and Canadian flag carriers in the U.S.-Toronto market. The competition that U.S. carriers offer to Canadian flag carriers continues to be an especially important consideration.

We find that the selection of Continental and USAir will maximize competition with Canadian flag carriers in important local markets where they have initiated significant new services since the signing of the Agreement. Canadian flag carriers currently operate six daily roundtrip frequencies at Newark, five daily roundtrip frequencies at Washington, D.C. (National), and three daily roundtrip frequencies at Washington, D.C. (Dulles) (where there is currently no U.S. flag service). In addition, Continental and USAir, by using their significant hub structures to route traffic over major eastern gateways at Newark and Washington, D.C. (National), are in the best position among the applicants to maximize competition with Canadian flag carriers in their behind-gateway markets, given Canadian carriers' rapid expansion into eastern markets over the past sixteen months. The selection of Continental also offers the competitive benefit of introducing a U.S. flag carrier that does not serve Toronto with its own aircraft to the U.S.-Toronto market.

The selection of Continental and USAir will have the additional benefit of furthering intergateway and intragateway competition. Each carrier, by offering attractive service options to passengers and shippers with its developed hub structure and significant online connecting services, will provide considerable competition against both U.S. and Canadian carriers at other gateways. In addition, Continental will provide head-to-head competition against Air Canada, Canadian Airlines International, and American Airlines in the huge New York market, while USAir will offer head-to-head U.S.-flag competition against Air Canada at Washington, D.C. (National).

Midway and the Raleigh-Durham Airport Authority and Northwest argue that the selection of USAir will increase the concentration of U.S. carrier service at Toronto. Under the circumstances of this case, the fact that up to four more carriers will be able to enter the U.S.-Toronto market in less than eight months, and an unlimited number of carriers will be free to enter the market one year after that, in February 1998, makes us less concerned that there will be undue concentration of U.S. carriers in this market.

Given the opening of the U.S.-Toronto market that is to occur in the months ahead, we are not persuaded by Midway's and the Raleigh Durham Airport Authority's arguments that fostering new entry should be the primary decisional factor in this case. We are also unpersuaded that insertion of an additional U.S. carrier (the ninth) in the U.S.-Toronto market now should be, in itself, a determinative public interest benefit, given the certainty of further opportunities for new entrant carriers in the months ahead. Midway and the Raleigh-Durham Airport Authority argued that failure to insert an additional carrier in the market now will make it even more difficult for new entrants to enter the market in the future; however, they offered no compelling reasons why this should be the case.

Although the subject is discussed at some length in Northwest's objection, the grant of exemption authority to USAir at Washington National as an accelerated second-year selection under the Agreement is not relevant in this proceeding, contrary to Northwest's assertions. The fact that USAir

was awarded exemption authority has in no way influenced the outcome of this case, consistent with longstanding Department policy and practice. Furthermore, as we stated in Order 96-2-45, special treatment of Washington, D.C. (National) in the Agreement recognizes only the importance of maintaining a strong U.S. flag presence in that market. Northwest has not persuaded us that a strong U.S. flag presence at Washington D.C. (National) is any less important now than it was when the Agreement was signed in February of last year.

Backup authority

None of the parties disputed the tentative award of backup authority in Order 96-5-21, and we will therefore make final our tentative conclusions supporting that award. Selecting Northwest to serve Minneapolis/St. Paul-Toronto as a backup to both Continental and USAir offers the potential of extending the benefits of a Toronto gateway to an established player in the Toronto market -- a helpful factor in the backup context -- with a strong U.S. hub. In addition, it would provide intergateway competition with TWA at St. Louis and American and United at Chicago, while adding new nonstop seats in a local U.S.-Toronto market in competition with Air Canada. At the same time, Northwest would provide online connecting service to a number of western points. Given Northwest's existing service at both Minneapolis/St. Paul and Toronto, it is well positioned to begin service should the selected primary carriers not institute service or discontinue operations.

Dormancy Provisions

As we previously indicated, in order to maximize the use of scarce bilateral route authority, the temporary, experimental certificates issued here will include 45-day dormancy provisions. The dormancy provisions act to cause the authority to expire automatically and therefore be available for award to another carrier if service is not provided for a 45-day period. No carrier opposed the inclusion of such a provision, although we specifically invited comment on the issue.

Accordingly,

1. We hereby make final our tentative findings and conclusions awarding certificate authority to Continental Air Lines and USAir to operate two daily round-trip scheduled combination frequencies each, Continental between Newark and Toronto and USAir between Washington, D.C. (National) and Toronto. We also make final our tentative grant of backup authority to Northwest (as backup to both Continental and USAir) to operate two daily round-trip scheduled combination frequencies between Minneapolis/St. Paul and Toronto;
2. We will not entertain Petitions for Reconsideration of this order;
3. To the extent not granted, we deny all other requests in this proceeding;
4. Unless disapproved by the President of the United States under 49 U.S.C. section 41307, this order and the attached certificates shall become effective on the 61st day following its submission for section 41307 review, or upon the date of receipt of advice from the President or his designee under Executive Order 12597 and implementing regulations that he or she does not intend to disapprove the Department's order under that section, whichever occurs earlier⁵ and
5. We shall serve this order on all parties in Docket OST-95-782, and the Canadian Ambassador, Department of State (Office of Aviation Negotiations), and the FAA.

⁵ This order was submitted for section 41307 review on _____, 1996. On _____, 1996, we received notification that the President's designee under Executive Order 12597 and implementing regulations did not intend to disapprove the Department's order.

By:

PATRICK V. MURPHY
Deputy Assistant Secretary for
Aviation and International Affairs

(SEAL)

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